COMMENTARY

Where is the light at the end of the tunnel?

We've made it through March, the 15th month of this recession. If the recession lasts into May, it will be the longest one since the Great Depression. Is anyone having fun yet?

VIEWPOINT
ANDREW BROD

By this point in a typical recession, economists start noticing glimmers of light at the end of the tunnel, as some economic indicators begin to turn positive. One of the strongest indications is when the number of initial claims for unemployment insurance starts declining. In addition, manufacturing begins to perk up, housing starts begin to rise and the index of consumer confidence shows signs of life.

But so far, very little is glimmering. Weekly unemployment claims have fallen slightly since late February, but they're still well above 600,000 and higher than at any time since 1982. Also in February, consumer confidence hit another all-time low and industrial production fell further.

And housing? I don't think anyone expects that industry to lead us out of this recession. Both existing-home sales and housing starts rose in February, but the former was largely due to distressed sales and the latter is still only about a quarter of what it was four years ago.

We've seen declines in payrolls, factory orders and service-sector activity. The index of leading economic indicators dropped in February, which suggests that the good news is still at least a few months away.

And unemployment continues to rise. The national rate hit a seasonally adjusted 8.1 percent in February, the highest it's been since 1983. In North Carolina, the rate rose to an alarming 10.3 percent in January, but some of that was the result of seasonal factors: the adjusted rate was "only" 9.7 percent.

The state doesn't adjust local rates, but my colleague Don Jud does, and he calculated the seasonally adjusted January rate in the Triad as 8.7 percent, up from 5 percent a year ago.

The only good news we've seen has been sporadic or misleading. There were upward blips in consumer spending and personal income, but it's too soon to place much weight on those numbers. Retail sales were down less than expected in February, which is what passes as good news these days. But hey, furniture sales rose in February for the first time since last May.

Why is good news so rare this late in the recession? In part, it's because of the official dating of this recession. What we're experiencing is really a recession-within-a-recession. From December 2007 until last fall, we had a mild downturn, as employment declined but most other indicators held steady. Then the financial crisis slammed the economy with a vengeance, and that's when things got really bad.

The financial crisis began in earnest after the investment bank Lehman Brothers failed in mid-September. Using that date, we're only about six months into the deep recession that built on and exacerbated the mild recession then under way. Perhaps we shouldn't expect to be over the hump yet in this recession-within-a-recession.

We haven't seen this combination of deep recession and financial crisis since the 1930s. Even though the economic pain of this recession won't approach that of the Great Depression, our situation is still quite serious. But with luck, the combination of fiscal stimulus, financial stabilization and the basic resiliency of the American economy will make it possible for more glimmers of light to start shining our way.

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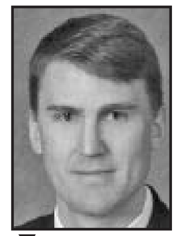
Obama should seek alternative to cap-and-trade

President Obama's proposed budget promises to reverse "an era of profound irresponsibility." The budget identifies energy policy as one of the many areas in need of change. Our government should pursue important goals such as preserving the environment and reducing dependence on foreign oil to improve national security. Unfortunately, the president's proposal to enact a cap-and-trade system to limit carbon emissions takes the wrong approach.

In a cap-and-trade system, the government would first determine the maximum amount of carbon emissions permitted. This sets the "cap." The government would then auction off "allowances" to companies that emit carbon. An allowance authorizes its owner to release a certain amount of carbon into the atmosphere. Allowances would be tradable and their value would fluctuate based on changes in demand. This would allow market conditions to determine how much it costs to emit carbon.



GUEST COLUMN
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The budget projects that money brought in from auctioning allowances will provide enough revenue to fund $15 billion in "clean energy technologies" and $60 billion in tax credits for working families annually through 2019. This would wean us from our current dependence on foreign oil and provide much-needed tax relief to middle- and lower-income families. Sounds good so far.

But there are major downsides to the proposal. First, cap-and-trade will cause a significant increase in energy costs. Carbon emitters will pay for allowances by passing the cost through to consumers. Who will be purchasing the allowances? Among others, utility providers. This means that we can expect to see significant increases in our electricity bills.

The Obama administration acknowledges this problem and responds by pointing to the annual $60 billion in tax credits that it intends to return to taxpayers as a way of mitigating the increased energy costs. This is called revenue recycling. The government institutes a policy that results in an increased cost to consumers, but then returns at least some of that increased cost in the form of a tax break. The question is whether the tax break will match the cost increase.

A second major problem is complexity. The cap-and-trade system requires that the government establish a totally new regulatory regime. This regime will have to combine technical monitoring (to make sure that emitters don't exceed their permitted allowances) with securities regulation (to oversee trading of the allowances). In effect, allowances are like tradable securities, only more complicated. Given the government's recent performance in regulating markets, can we have total faith that a new regulatory regime will succeed?

The government should dump the cap-and-trade proposal and simplify. Cap-and-trade is really just a tax wrapped up in the more politically palatable jargon of "market-driven" regulation. If the government needs to reduce carbon emissions, then it should be honest with taxpayers and simply enact a carbon tax. A tax could be structured to bring in the same revenues as cap-and-trade and would eliminate the unnecessary bureaucracy and uncertainty inherent in creating a trading system.

Unfortunately, taxes aren't politically feasible. That's why we're likely to be saddled with another bloated and ineffective regulatory agency to monitor a new cap-and-trade system. We can only hope that when it comes to regulating a complex trading system, the government's past performance is no indication of future results.

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